IN THE

Supreme Court of the United States

October Term, 1946
No. 365

EDWARD R. DOWNING, suing on his own behalf, and on behalf of all other stockholders of THE UNITED CORPORATION (of Delaware), etc.,

Petitioner,

against

GEORGE H. HOWARD, *et al.*,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF

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To the Honorable Chief Justice of the United States and the Honorable Associate Justices of the Supreme Court of the United States:

Your Petitioner respectfully shows:

Summary Statement of Matter Involved

Petitioner is a stockholder of The United Corporation (of Delaware), hereafter referred to as United. He brought this action in August 1944 in the United States District Court for the District of Delaware (R. 1a) on behalf of himself, other stockholders of United, and the corporation, against individuals (or in some instances, the personal representatives of their estates) who were or had been

officers or directors of United or had been members of banking firms or companies alleged to have controlled the directors and conspired with them for their own profit and to the damage of the corporation and its stockholders. The unlawful acts complained of consisted of willfully causing the corporation to do certain acts in violation of the provisions of Sections 4(a) and (b) and 11(e) of the Public Utility Holding Company Act of 1935 (hereafter referred to as the Act).

All but three of the individual defendants are non-residents of Delaware and were served with process outside of that state (R. 4a, 6a, 7a, 8a). Petitioner concedes that such service was not effective unless this is an action based on the Public Utility Holding Company Act of 1935, Section 25 of which expressly provides for such extra-territorial service. Petitioner also concedes that he is not properly in a federal court if his action does not arise under that Act, since there is no diversity of citizenship between Petitioner and three of the defendants.

The defendants moved to dismiss the action on some or all the defenses numbered (1) to (5) of Rule 12(b) of the Federal Rules of Civil Procedure (R. 73a, 75a, 77a, 79a, 80a, 82a, 84a, 86a, 87a, 89a, 91a, 93a, 95a, 97a, 99a, 101a). The District Court granted the motions to dismiss on the ground that it lacked jurisdiction over the subject matter of the action (R. 126a-139a, 144a-146a) and the Circuit Court of Appeals for the Third Circuit affirmed the dismissal on that ground (R. fol. 152a). Neither court therefore found it necessary to pass upon the questions raised by defendants' motions as to the propriety of the venue of the action or the effectiveness of the service of process on

those non-resident defendants who were the representatives of the estates of deceased directors, assuming that the action was properly based on the Public Utility Holding Company Act of 1935.

The Amended Complaint

The defendants' motions were directed to the Amended Complaint, filed in August 1945, which sets forth the following facts in three separate causes of action (R. 11a-70a).

First Cause of Action

The United Corporation was incorporated under the laws of Delaware in 1929. Its principal organizers were J. P. Morgan & Company, whose partners are named as defendants in this action, the defendant Landon K. Thorne, Bonbright & Company, Inc. (now known as Commercial Enterprises Corporation, a defendant herein), Bonbright Electrical Corporation (now known as Bonbright, Loomis & Company, Inc., a defendant herein) and the defendant Alfred L. Loomis, all of whom were at that time engaged directly or indirectly in the business of commercial and investment banking (R. 13a, 14a, 21a). From the time of the organization of United in 1929 until August 1945, when the Amended Complaint was filed, through control of the proxy committee and ownership of substantial amounts of outstanding voting stock of United, and also by agreement with various persons directly and indirectly owning large amounts of outstanding voting stock of United, the defendants above referred to elected the Board of Directors of United, and dominated and controlled the manage-

ment and policies of United and of the various subsidiary holding companies and operating companies in the United holding-company system (R. 20a-22a).

On August 26, 1935, the Public Utility Holding Company Act of 1935 became law. United, its four principal subsidiaries and many of its sub-sidiaries, were holding companies as defined in that Act. Section 4(a) made it unlawful after December 1, 1935, for any holding company, unless it registered under Section 5, to perform any of the acts enumerated in Section 4(a). United, in fact, did not register under Section 5 at any time from the passage of the Act until March 28, 1938. On that date it registered (R. 23a-29a).

Section 4(a) expressly made it unlawful for an unregistered holding company "to own, control or hold with power to vote, any security of any subsidiary company. * * *" The defendants nevertheless caused United, while unregistered, to continue to own, control and hold with power to vote the securities of its subsidiary companies (R. 29a, 30a). The reason that the defendants caused United to continue to hold these securities was to enable the controlling banking interests referred to above to continue to realize profits after December 31, 1935, as they had prior to that date, through the instrumentality of United. For prior to that date J. P. Morgan & Company had realized net profits of over $19,000,000, and Landon K. Thorne, Bonbright & Company, Inc. and Alfred K. Loomis directly and indirectly had realized profits of approximately $18,000,000 from fees, interest, loans and transactions in the securities of United. By causing United to continue to own these securities of its subsidiaries, the

defendants continued their domination and control over the United holding-company system and thereby were enabled to continue to make substantial profits during the period December 1, 1935 to March 28, 1938, while United was unregistered. J. P. Morgan & Company profited from the deposit of moneys with it by companies in the United system, including moneys derived by the companies from sale of their securities to underwriters, the total amount of such securities underwritten during this period amounting to approximately $479,000,000. In addition, the partners of J. P. Morgan & Company profited through their stock ownership in Morgan, Stanley & Co., Inc., which received underwriting fees from companies in the United system amounting to more than $2,000,000 (R. 32a-34a).

Apart from the profits realized by the defendants, their action in causing United to continue to own the securities of its subsidiaries resulted in great damage to the stockholders of United. The market value of the securities of the subsidiaries which United owned on December 1, 1935, amounted to approximately $194,000,000. On March 28, 1938, this value had decreased to $107,000,000, a loss of value amount approximately to $87,000,000. The value of the securities in August, 1945, when the Amended Complaint was filed, was still far below that of December 1, 1935 (R. 36a).

During the thirteen months following December 1, 1935, it would have been possible for United to divest itself of these securities and realize a sum approximating their December 1, 1935 market value, or to distribute its securities to its stockholders by way of dissolution or reorganization. In addition, between December 1, 1935 and March

28, 1938, United expended approximately $1,000,000 in salaries, legal and auditing fees, taxes, and other business and administration expenses arising out of its retention of ownership of the securities of its subsidiaries during this period in violation of Section 4(a) of the Public Utility Holding Company Act of 1935 (R. 31a, 36a).

Second Cause of Action

In February 1937, United owned 1,914,417 shares of the outstanding voting common stock of Niagara Hudson Power Corporation, and approximately 62,370 shares of the outstanding voting second preferred stock of Mohawk Hudson Power Corporation. Niagara was a subsidiary of United and Mohawk was a subsidiary of Niagara (and also of United) (R. 40a, 41a).

Under a proposed plan to consolidate Mohawk and Niagara into a new corporation called Consolidated Niagara Hudson Power Corporation, the holders of Mohawk second preferred stock were given a choice of exchanging one share of stock either for seven shares of Consolidated Niagara common stock or for one share of Consolidated Niagara 5% second preferred and 1½ shares of Consolidated Niagara common stock. Acceptance of the seven shares of Consolidated Niagara common required waiving rights to dividends which had accumulated for three years prior to February 1, 1937, on the Mohawk second preferred. The plan further provided that if a holder of Mohawk second preferred did not choose either option, he would automatically receive one share of the Consolidated Niagara 5% cumulative second preferred, carrying a right to a special dividend equivalent to the dividend accumu-

lated on the Mohawk second preferred. The defendants caused United to vote its shares of stock in favor of the consolidation. The plan could not have been approved by the required percentage of stock without the votes of the stock owned by United. The defendants also caused United to elect to exchange its shares of Mohawk second preferred on the basis of one share of that stock for seven shares of Consolidated Niagara common, with the result that United acquired 436,590 shares of Consolidated Niagara common stock. The foregoing acts of exchanging securities, negotiating for the acquisition of and acquiring said shares of Consolidated Niagara common stock were, to the knowledge of the defendants, in violation of Section 4(a)(3) and (4) of the Act (R. 40a, 41a).

If United had not elected to acquire such shares of Consolidated Niagara common, it would have received, by automatic operation of the plan of consolidation, one share of Consolidated Niagara second preferred, carrying the special dividend rights referred to above, for each share of Mohawk second preferred which it had owned. The dividends that United waived by making the election which it did amounted to approximately $935,550. Dividends of that character were in fact paid by Consolidated Niagara subsequent to 1936 to those holders of Mohawk second preferred who did not make either election and who consequently received Consolidated Niagara second preferred together with the special dividend rights (R. 42a-44a).

Furthermore, dividends of $5.00 a year have either been paid or have accumulated on the Consolidated Niagara second preferred from 1937 to the present time. This would have amounted to $311,850 a year on the 62,370 shares of

Consolidated Niagara second preferred, which United would have received or become entitled to if it had refrained from making the affirmative election which it did. The 436,590 shares of Consolidated Niagara common stock acquired and still owned by United now have a market value of approximately $1,309,900 as compared with a present market value of $4,241,000 for the 62,370 shares of Consolidated Niagara second preferred which United would have received under the automatic provisions of the consolidation plan. Furthermore, the value of the common shares of Consolidated Niagara has substantially diminished with the result that the total value of United's 436,590 shares of that stock is far below the February 1937 value of the 62,370 shares of Mohawk stock which United gave in exchange therefor (R. 43a, 44a).

Third Cause of Action

The defendants other than United caused United to fail to register with the Securities and Exchange Commission from December 1, 1935 to March 28, 1938, although it was required to register by Section 4(b) of the Act. On March 28, 1938 it registered (R. 29a).

Section 11(e) authorized any registered holding company at any time after January 1, 1936 to submit a plan to the Securities and Exchange Commission for the divestment of control, securities or other assets, or for other action for the purpose of enabling such company to comply with the provisions of Section 11(b).

Between 1936 and the date of the filing of the Amended Complaint, United contributed nothing to the normal functioning of its system companies, and its continued existence

unduly and unnecessarily complicated the structure of the system. United rendered no public utility or other services to its system companies, its chief business function being merely to hold the securities of its subsidiaries and certain other corporations. For these reasons United was required by Section 11 to cease to be a holding company and it was the duty of its directors to cause United to cease to own 10% of the stock of its subsidiaries. Nevertheless, United took no steps to insure that its corporate structure and existence did not unduly or unnecessarily complicate the structure of its holding company system, and United did not cease to hold and own the voting stock of its subsidiaries, although it could have done so (R. 52a-54a).

On March 4, 1941, United did file an application with the Commission under Section 11(e) for approval of an alleged "plan" for divestment of control and securities of subsidiaries, but the Commission, after hearings held between November 17, 1941 and January 18, 1942, issued an order dated August 14, 1943, disapproving the purported plan and directing United to cease to be a holding company. The defendants, nevertheless, caused United to continue to own more than 10% of the outstanding voting shares of its subsidiaries (R. 52a-55a).

The reason the defendants caused United to continue to own the securities of its subsidiaries and to fail to file a plan, was in order to enable the defendant banking interests to continue to realize profits as they had in the past, through the instrumentality of United. Between January 1, 1936 and the filing of the Amended Complaint in August 1935, the value of the securities owned by United in its subsidiaries decreased approximately $87,000,000. In ad-

dition, United expended considerable sums in payment of salaries, legal and auditing fees, taxes, and other business expenses, all arising out of its continued retention of ownership of the securities of its subsidiaries (R. 56a-60a).

Questions Presented

1. Does the Public Utility Holding Company Act of 1935 give a stockholder of a public utility holding company a right of action against its officers and directors, and affiliated banking interests who controlled them, for damages and profits resulting from their actions in willfully causing such company, while unregistered, to own the securities of subsidiary companies, in violation of the express prohibition contained in Section 4(a)(6)?

2. Does the Public Utility Holding Company Act of 1935 give a stockholder of a public utility holding company a right of action against its officers and directors, and affiliated banking interests who controlled them, for damages and profits resulting from their actions in willfully causing such company, while unregistered, to exchange the securities of subsidiary companies, in violation of the express prohibitions contained in Section 4(a)(3) and (4)?

3. Does the Public Utility Holding Company Act of 1935 give a stockholder of a public utility holding company a right of action against its officers and directors, and affiliated banking interests who controlled them, for damages and profits resulting from their actions in willfully causing such company to fail to register pursuant to the provisions of Section 4(b) until March 28, 1938 and, after

it registered on that date, to fail to file a plan under Section 11(e) for the divestment of control, securities or other assets, or for other action enabling the company to comply with the provisions of Section 11(b), where the company is economically unnecessary and performs no services for its system companies?

The Petitioner contends that all three questions should be answered in the affirmative. The District Court and the Circuit Court of Appeals below answered them all in the negative. Even if Petitioner's position is correct as to only one of these questions, it was error for the courts below to dismiss the action.

Reasons Relied on for the Allowance of the Writ

1. The Circuit Court of Appeals has decided important questions relating to the interpretation of Sections 4(a), 4(b) and 11(e) of the Public Utility Holding Company Act of 1935 which have not been, but should be, settled by this Court.

Although in *Electric Bond & Share Co.* v. *Securities and Exchange Commission*, 303 U. S. 419, 442, this Court upheld the constitutionality of Section 4(a) in an action brought by the Securities and Exchange Commission, it has never had occasion to define the extent to which that section creates civil liability to private parties on the part of persons who willfully cause holding companies to violate its provisions. Nor has it ever determined whether Section 11(e) imposes any duty upon the directors of an economically unnecessary holding company, which fails to comply with the standards of Section 11(b), to cause such company to file a plan enabling it to comply with those

provisions. It is believed that these are matters of great importance both to investors in the securities of public utility holding companies and to the officers and directors of such companies.

2. The Circuit Court of Appeals has decided questions of interpretation of Section 4(a) in a way probably in conflict with applicable decisions of this Court.

By holding that directors who cause an unregistered holding company to do acts expressly proscribed by statute which result in damage to persons indisputably within a class intended to be protected by such statute, are not civilly liable to such persons, the decision of the Circuit Court of Appeals appears to be in conflict with the decision enunciated by this Court in *Texas & Pacific R.R.* v. *Rigsby*, 241 U. S. 33. In that case it was held that the disregard of a statute is an unlawful act and that where it results in damage to a member of a class for whose especial benefit the statute was enacted, the right to recover in a civil action is implied, even though the statute does not expressly provide for a civil right of action.

3. The decision of the Circuit Court of Appeals is in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in the case of *Goldstein* v. *Groesbeck, et al.*, 142 F. 2d 422 (C. C. A. 2, 1944), cert. den. 323 U. S. 737.

In that case the Circuit Court of Appeals for the Second Circuit held that the Public Utility Holding Company Act of 1935 gave a stockholder of an intermediate holding company a right of action against the top holding company and its officers and directors based on service and

construction contracts made by the top holding company, while unregistered, in violation of the prohibition against such contracts contained in Section 4(a)(2). The ground of the Court's decision was that the Act would be not only "sadly wanting" but "delusive" if it did not provide a private right of action "to those for whose ultimate protection" the statute was intended. See *Goldstein* v. *Groesbeck, supra,* at p. 427. Although the opinion below of the Circuit Court of Appeals for the Third Circuit did not express any disagreement with the decision in that case, it is Petitioner's position that the bases of the decisions are in conflict and necessarily lead to conflicting conclusions as to the extent of civil liability to private parties under Section 4(a).

4. The case involves important questions relating to the interpretation of the provisions of Section 25 of the Public Utility Holding Company Act of 1935 dealing with venue and jurisdiction over the person, which have not been, but should be, settled by this Court.

Assuming that, as Petitioner contends, the Amended Complaint sets forth valid claims under the Act, the defendants' motions attack the propriety of the venue of the action and the effectiveness of the service of process beyond the territorial limits of Delaware on non-resident defendants who are the representatives of decedents' estates. The Courts below found it unnecessary to pass upon these questions in view of their conclusions that the action was not based on the Act; but if, as Petitioner contends, these conclusions are incorrect, it will be necessary to determine these questions in order to make a complete disposition of this case.

It is Petitioner's position that the action was properly brought in the District of Delaware (under Section 25 of the Act, which provides for the bringing of an action "in the district wherein any act or transaction constituting the violation occurred") because the acts of United in owning and exchanging securities in violation of Section 4(a) took place in Delaware, the State of United's incorporation and in which it had its principal place of business, and because the acts of United were attributable to the defendants who caused United to commit such acts. The Memorandum filed by the Securities and Exchange Commission as *amicus curiae* in the Circuit Court of Appeals agreed that the venue of the action was proper, and also agreed that the service of process pursuant to Section 25 was effective in giving the District Court jurisdiction over the persons of non-resident defendants who were the executors or trustees of decedents' estates.*

WHEREFORE, Petitioner prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the United States Circuit Court of Appeals for the Third Circuit commanding that Court to certify to and send to this Court for its review and determination a full and complete transcript of the record and of the proceedings of said Court had in the case numbered and entitled in its docket as "No. 9314, Edward R. Downing, etc., Appel-

* The Commission's Memorandum was submitted "with respect to certain of the issues raised by this appeal which present important questions as to the construction of the Public Utility Holding Company Act of 1935;" but, in conformity with its general policy of avoiding participation in private litigation concerning violations of Section 4, the Commission expressly refrained from taking any position on the question whether the Amended Complaint stated valid claims based on Section 4(a)). *Memorandum of Securities and Exchange Commission, Amicus Curiae*, pp. 1, 2.

lant, v. George H. Howard, et al." and that the judgment of said Court, affirming the judgments of the United States District Court for the District of Delaware, be reversed by this Court.

Dated: September 22, 1947.

EDWARD R. DOWNING,
Petitioner.

By JAMES R. MORFORD,
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JOHN F. DAVIDSON,
Of Counsel.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTORARI

Opinions of Courts Below

The opinion of the Circuit Court of Appeals (R. fol. 152a) is not yet reported. The opinion of the District Court (R. 126-139a, 144a-146a) is reported in 68 F. Supp. 6.

Jurisdiction

The judgment of the Circuit Court of Appeals was entered June 24, 1947 (R. fol. 152a). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. 347).

Statement of the Case

The statement at pages 1-11 of the preceding petition is hereby adopted and made a part of this brief.

Specifications of Error

1. The Circuit Court of Appeals erred in holding, as to the "First Cause of Action," that:

(a) In order for a complaint by a stockholder of an unregistered public utility holding company to state a valid claim based on violation of Section 4(a)(6) of the Public Utility Holding Company Act of 1935, it must allege that the damages to such company's stockholders resulted from the company's "failure to register" under Section 5, rather than from its ownership of securities of subsidiaries in violation of the express prohibition of Section 4(a)(6).

(b) A complaint in a derivative action brought by a stockholder of an unregistered holding company against its officers and directors can not state a valid claim under Section 4(a)(6) unless it alleges as a fact that the damages complained of would not have occurred if the holding company had been a registered holding company.

(c) Ownership of securities of its subsidiaries by an unregistered holding company in violation of Section 4(a)(6) is not the legal cause of damage to the stockholders of such company where the decline in the value of such securities is not alleged to be the result of the holding company's failure to register.

(d) In effect, the *only* purpose of Section 4(a) was to compel holding companies to register.

(e) A complaint fails to state a valid claim based on Section 4(a)(6) even though it alleges that the directors of a holding company, and affiliated banking interests who controlled them, realized profits as the result of causing the company, while unregistered, to own the securities of subsidiaries, in violation of that section.

(f) Causing an unregistered holding company to own securities in violation of Section 4(a)(6) is not the legal cause of damage to stockholders of such company unless its directors are held liable as insurers against all harm.

(g) A complaint which is defective in any of the foregoing respects should be dismissed for lack of jurisdiction over the subject matter of the action.

2. The Circuit Court of Appeals erred in holding, as to the "Second Cause of Action," that:

(a) The exchange of securities of its subsidiaries by an unregistered holding company in violation of Section 4(a)(3) and (4) is not the legal cause of damage to the stockholders of such company where the complaint does not allege as a fact that the loss resulting from such exchange would not have occurred if such company had been a registered holding company.

(b) In order for a complaint to state a valid claim under Section 4(a)(3) and (4), it must allege that the loss resulting from an exchange effected by an unregistered holding company in violation of the provisions of that section was caused by the holding company's failure to register.

(c) Causing an unregistered holding company to exchange securities of its subsidiaries in violation of Sections 4(a)(3) and (4) is not the legal cause of damage to stockholders of the company, unless its directors are held liable as insurers against all harm.

(d) Even if a complaint alleged that an exchange of securities of subsidiaries prohibited by Section 4(a)(3) and (4) would never have taken place if the holding company had been registered, it would still be legally insufficient unless it stated facts to show that the resulting loss to stockholders of the company happened in a way which the statute was enacted to prevent.

(e) A complaint which fails to contain any of the foregoing allegations should be dismissed for lack of jurisdiction over the subject matter of the action.

3. The Circuit Court of Appeals erred in holding, as to the "Third Cause of Action," that:

(a) Section 11(e) imposes no duty upon officers and directors of an economically unnecessary registered holding company, which renders no services to its system companies and whose structure does not conform to the standards of Section 11(b), to file a plan of divestment or control, or for the purpose of bringing the company into compliance with the provisions of Section 11(b).

4. The Circuit Court of Appeals erred in failing to hold that if the Amended Complaint states one or more valid claims under the Public Utility Holding Company Act of 1935, the District Court has jurisdiction over the persons of non-resident defendants who are the representatives of

decedents' estates as well as over the persons of the other individual defendants.

5. The Circuit Court of Appeals erred in failing to hold that if the Amended Complaint states one or more valid claims under the Public Utility Holding Company Act of 1935, the venue of the action is properly laid in the District of Delaware.

ARGUMENT

Summary of Argument

First and Second Causes of Action

Section 4(a) expressly makes it unlawful for an unregistered holding company to own or to exchange the securities of subsidiary companies. The law is settled that where a statute is enacted for the protection of a certain class of persons, a member of that class who is injured as the result of a violation of the statute may recover damages from the violator even though the statute does not expressly provide for a civil right of action. It is also settled that the directors of a corporation who cause it to violate a statute are individually liable for damages resulting from such violation. Petitioner, a stockholder of a public utility holding company, is a member of a class which the Act was designed to protect. He was injured by the willful acts of the directors of United in causing United, while unregistered, to own and to exchange the securities of subsidiary companies in violation of Section 4(a). Petitioner therefore has a right of action against the directors of United based on violations of Section 4(a) even though that section does not expressly provide for a civil action.

It was error for the Circuit Court of Appeals to limit the creation of a right of action for violation of Section 4(a) to cases in which the damages result from failure to register under Section 5. This conclusion is based upon the incorrect assumption that the *only* purpose of Section 4(a) was to cause holding companies to register. Both the Act itself and its legislative background show that Section 4(a) was intended to proscribe to unregistered holding companies the acts therein enumerated because such acts by unregistered holding companies were regarded as substantive evils in themselves and not merely because it was intended to exert pressure on such companies in order to cause them to register.

The acts done in violation of Section 4(a) were the legal cause of the damage to the Petitioner since the acts which violated the statute caused the injury to petitioner and resulted in profits to the defendants.

The decision of the Circuit Court of Appeals below permits the defendants to retain the fruits of their unlawful conduct and gives no relief to the stockholders injured by that conduct.

Third Cause of Action

The Act enlarged the fiduciary obligations of directors of holding companies and required that they act for the best interests of security holders as envisaged by the Act rather than in the interests of affiliated banking interests who dominated and controlled them. A stockholder in a registered holding company therefore has a right of action against directors who fail to perform the duty imposed upon them by Section 11(e) to file a plan of divestment and

control or for the purpose of bringing the company into compliance with the provisions of Section 11(b), where the holding company is economically unnecessary and renders no services to its system companies.

Jurisdiction

Since Petitioner has a right of action based on violations of Sections 4(a) or (b) or 11(e), the District Court has jurisdiction over the subject matter of the action under Section 25 of the Act and Petitioner was entitled to avail himself of the provisions of that section relating to venue and service of process.

POINT I

The Public Utility Holding Company Act of 1935 gives a stockholder of a holding company a right of action against the directors of such company for damages and profits resulting from their willful acts in causing the company, while unregistered, to own securities and to exchange securities of subsidiary companies in violation of the express prohibitions contained in Section 4(a) of the Act.

A. It was the clear and unequivocally expressed intention of Congress to forbid unregistered holding companies to own or exchange the securities of subsidiary companies or to do any of the other acts expressly proscribed by Section 4(a).

Section 4(a) provides, in part, that "unless a holding company is registered under Section 5, it shall be unlawful for such holding company, directly or indirectly * * * to distribute or make any public offering for sale or exchange of any security of such holding company, any subsidiary

company or affiliate of such holding company, any public utility company or any holding company" or "* * * to acquire or negotiate for the acquisition of any security or utility assets of any subsidiary company" or "to own, control or hold with power to vote any security of any subsidiary companies thereof * * *." It is too clear to require argument that the Congress intended by the foregoing language that no unregistered holding company should do any of the acts so proscribed. Section 29 makes willful violation of Section 4(a) a crime.

B. Under settled principles of law, a private right of action exists for violation of Section 4(a) even though that section does not expressly confer a civil right of action on private parties.

It has long been established that where a statute makes certain conduct unlawful, a person who is of the class intended to be protected and who has sustained damage from acts done in violation of the statute may maintain an action therefor, despite the absence of an express provision in the statute conferring a right of action for such violation. *Texas & Pacific R.R.* v. *Rigsby,* 241 U. S. 33; *Goldstein* v. *Groesbeck, et al.,* 142 F. 2d 422, 427 (C. C. A. 2, 1944), *cert. den.* 323 U. S. 737; *Zajkowski* v. *American Steel & Wire Co.,* 258 F. 9 (C. C. A. 6, 1918); *Armour* v. *Wanamaker,* 202 F. 423 (C. C. A. 3, 1913); *Baird* v. *Franklin,* 141 F. 2d 238, 244-245 (C. C. A. 2, 1944), *cert. den.* 323 U. S. 737; *Narramore* v. *Cleveland, C. C. & St. L. Ry. Co.,* 96 F. 298 (C. C. A. 6, 1899); see *Restatement of Torts,* §§286-288. It is also established that where the directors of a corporation cause it to violate a statute they are themselves liable under the statute, both civilly and criminally,

for their actions in causing such violation. *Northwest Theaters Co.* v. *Hanson,* 4 F. 2d 471 (C. C. A. 9, 1925); *United States* v. *Van Schaick,* 134 F. 592 (C. C.); *People* v. *Knapp,* 206 N. Y. 373, 99 N. E. 841; *State* v. *Frazer,* 105 *Or.* 589, 209 P. 467; see 19 C. J. S. p. 272; 3 *Fletcher Cyclopedia of Corporations,* §1137; cf. *Hitchcock* v. *American Plate Glass Co.,* 259 F. 948 (C. C. A. 3, 1919); *National Cash Register Co.* v. *Leland,* 94 F. 502 (C. C. A. 1, 1899); *U. S.* v. *Snyder,* 14 F. 554 (C. C.).

In *Goldstein* v. *Groesbeck, supra,* a stockholder of American Power & Light Co., which dominated and controlled four subsidiary operating companies, and was itself dominated and controlled by Electric Bond & Share Company, brought a double derivative stockholder's action on behalf of American's four operating companies against Electric Bond & Share, Ebasco Services (a subsidiary service company of Electric Bond & Share) and certain officers and directors of those companies, for an accounting of profits received by Ebasco under service and construction contracts made with the operating companies in violation of Section 4(a)(2) of the Act, while Electric Bond & Share Company was unregistered. Section 4(a) prohibits unregistered holding companies from entering into service or construction contracts with public-utility companies, just as it prohibits unregistered holding companies from owning or exchanging securities of subsidiary companies. In reversing the District Court's dismissal of the action against the defendants, the opinion of the Circuit Court of Appeals expressly rejected the contention that because the proscription of service contracts by Section 4(a)(2) was made as a penalty for failure to register, it followed

that Section 4(a)(2) could not be enforced by a private party, and went on to state that "we think a denial of a private right of action to those for whose ultimate protection the legislation is intended leaves legislation highly publicized as in the public interest in fact sadly wanting, and even delusive, to that end."

In the present case Petitioner, as a stockholder of a public utility holding company, is unquestionably a member of a class which, as Section 1(b) declares, the Act was designed to protect. He was injured by the willful acts of the directors of United in causing United, while unregistered, to own and to exchange the securities of subsidiary companies, in violation of Section 4(a). It is submitted, therefore, that Petitioner has a right of action against the directors of United based on violations of Section 4(a) even though that section does not expressly provide for a civil action.*

C. It was error for the Circuit Court of Appeals to limit the creation of a right of action for violation of Section 4(a) to cases in which the damages result from failure to register under Section 5.

1. *Causing Holding Companies to Register Was Not the Only Purpose of Section 4(a).*

The Circuit Court of Appeals held that the first two causes of action of the Amended Complaint did not state valid claims based on Section 4(a) because they did not allege that the damages complained of resulted from "failure

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* Recovery has been permitted against statute violators even by persons who were not members of a class intended to be protected by such statute. See *Grey's Exec'r.* v. *Mobile Trade Co.*, 55 Ala. 387; cf. *Union Pacific Railway Co.* v. *McDonald*, 152 U. S. 262, 282.

to register'' under Section 5 (R. fol. 152a, Opinion of C. C. A., p. 10). This is a limitation upon the liability which would normally follow from the violation of such a statutory provision, under the principles discussed above. No such limitation was placed upon liability for violation of Section 4(a) by the decision in *Goldstein* v. *Groesbeck, supra.*

Of course, Congress may limit or entirely withhold the right to recover damages resulting from a statutory violation. But, as stated in *Kardon* v. *National Gypsum Company, et al.,* 69 F. Supp. 512, 514 (E. D. Pa.), ''the right is so fundamental and so deeply ingrained in the law that where it is not expressly denied the intention to withhold it should appear very clearly or plainly.'' In the present case there is no provision in the Act which either withholds a private right of action for violation of Section 4(a) or limits such right to situations in which the damages caused by such violation resulted from failure to register under Section 5.*

The Circuit Court of Appeals' conclusion as to the existence of such limitation is based on the assumption that the *only* purpose of Section 4(a) was to compel holding companies to register. The only bases for this assumption referred to in the Court's opinion are the decision of this Court in *Electric Bond & Share Co.* v. *Securities and Exchange Commission,* 303 U. S. 419, 442, and comments in the Reports of the House and Senate Committees with ref-

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* Section 25 of the Act vests the District Court with "jurisdiction of violations of this title * * * and * * * of all suits in equity and actions at law brought to enforce any liability or duty created by * * * this title * * *''

erence to Section 4 (R. fol. 152a, Opinion of C. C. A., p. 5, footnote 18, p. 8).

In the *Electric Bond & Share* case this Court stated that the penalty for failure to register under Section 5 of the Act was the withdrawal from unregistered holding companies of the right to do any of the acts enumerated in Section 4(a). This penalty was incurred, therefore, only if an unregistered company complied with Section 4(a). But if it did not comply, as United did not comply, it did not suffer this penalty. The fact that refraining from doing the acts prohibited by Section 4(a) is the penalty for remaining unregistered is, therefore, entirely irrelevant to a determination of whether Congress intended a private party to have a civil right of action for acts which in fact were done by an unregistered company in violation of Section 4(a). The decision of this Court in the *Electric Bond & Share* case, therefore, lends no support to the assumption that the only purpose of Section 4(a) was to compel registration or the conclusion that Congress intended no right of action or only a very limited right of action for violation of that section. See *Goldstein* v. *Groesbeck, supra,* at p. 427.

The statement in the Committee Reports with reference to Section 4 reads as follows:*

> "SECTION 4. TRANSACTIONS BY UNREGISTERED HOLDING COMPANIES.
>
> This section establishes the mechanism by which holding companies are brought under the jurisdic-

* Sen. Rep. No. 621, 74th Cong. 1st Sess., p. 25; H. R. Rep. No. 1318, 74th Cong. 1st Sess., p. 11.

> tion of the Commission so that the provisions of title I may be effectively administered. That mechanism is registration, and it is made the duty of every holding company, unless exempted, to register by November 1, 1935, if it is to carry on any of the activities which are national in scope and hence of particular concern to the Federal Government. Unregistered companies after that date are prohibited from engaging in these activities unless they are registered."

It is apparent that the foregoing paragraph relates to Section 4 as a whole and not exclusively to Section 4(a). For Section 4(b) made it the duty of every holding company, unless exempted, to register if it was to carry on any of the activities of national scope which were of concern to the Federal Government. See *North American Co. v. Securities and Exchange Commission,* 327 U. S. 686, 697, footnote 8. The fact that the whole section established a mechanism which Congress contemplated would cause holding companies to register is not evidence that the only purpose of subdivision (a) of Section 4 was to compel registration. The "mechanism" of the section was to require all holding companies to register by Section 4(b) and to forbid any company which did not register to do any of the acts enumerated in Section 4(a). The fact that Congress probably contemplated that all companies would register rather than refrain from doing the acts prohibited by Section 4(a) is not persuasive that Congress intended either that no civil liability should attach to acts done by an unregistered company in violation of Section 4(a) or that such liability should be limited to cases in which the damages resulted from failure to register under Section 5.

The whole structure of the Act makes it apparent that Congress intended entirely different types of provisions to apply to unregistered holding companies than applied to registered holding companies. The former were completely prohibited from doing any of the acts enumerated in Section 4(a). The latter were subjected to the supervisory jurisdiction of the Securities and Exchange Commission and were permitted to do all of the acts enumerated in Section 4(a), provided they made the disclosures and complied with the requirements laid down by later sections of the Act and the Commission determined that the particular actions proposed conformed to the standards prescribed for registered holding companies. See *North American. Co.* v. *Securities and Exchange Commission, supra,* at pp. 697-698.

While it is clear that Congress intended that holding companies should register, it is equally clear that it intended that unregistered companies should not do any of the acts expressly prohibited by Section 4(a). The extensive investigations and reports made by the Federal Trade Commission and the House Committee on Interstate and Foreign Commerce, which preceded the passage of the Act, had shown the manifold and complex evils which had resulted from the ownership, acquisition and disposition of the securities of their subsidiaries by unregulated holding companies. These reports dealt at length with the injuries to investors in the securities of unregulated holding companies which had resulted from the management and control of such companies by officers and directors dominated

and controlled by banking concerns whose interests were in conflict with those of the company's stockholders. See Reports of Federal Trade Commission made pursuant to S. Res. 83, 70th Cong., 1st Sess., No. 52, pp. 1-86, 488-602; No. 72A, pp. 111-116, 130-136, 858-870, 880; No. 73A, pp. 61-64; Reports of the Committee on Interstate and Foreign Commerce, House of Representatives, made pursuant to H. Res. 59, 72nd Cong., 1st Sess., and H.J. Res. 572, 72nd Cong., 2nd Sess., Part 2, pp. 94-97, Part 5, pp. 717-751; S. Rep. No. 621, 74th Cong., 1st Sess. (to accompany S. 2796), p. 4. In the present case the Amended Complaint alleges that the reason why the defendant banking interests, through their control of the directors of United, caused United to own the securities of subsidiaries in violation of Section 4(a) was to enable them to continue to realize profits as they had in the past from their control of United and the subsidiary companies in its holding-company system.

Section 1(c) of the Act specifically states, on the basis of the abuses enumerated in Section 1(b), that "the holding company becomes an agency which unless regulated is injurious to investors * * *."

It is submitted that the foregoing makes it abundantly clear that Congress regarded the activities which Section 4(a) forbade to unregistered holding companies as substantive evils in themselves and that the purpose of the prohibition of such activities was not merely to exert pressure on unregistered holding companies in order to cause them to register.

It is therefore submitted that there is no evidence to support the assumption of the Circuit Court of Appeals that the only purpose of Section 4(a) was to compel holding companies to register, or its conclusion that Congress intended that civil liability for violation of Section 4(a) should be limited to cases where the damages resulted from failure to register. To the contrary, the Act's legislative background, entire structure and declaration of policy contained in Section 1 constitute affirmative evidence that Congress intended the normal rule of civil liability to be applied to violations of Section 4(a) without the restrictions imposed by the decision below of the Circuit Court of Appeals.

Moreover, it should be observed that the imposition of normal civil liability for violation of Section 4(a) is not inconsistent with the purpose of causing holding companies to register but is in aid of that purpose. For the imposition of such liability for violation of Section 4(a), in addition to the criminal and injunctive remedies of the Act, gives added weight to the pressure which Section 4(a) was designed to exert in order to cause holding companies to register.

As stated by Circuit Judge (later Chief Justice) Taft in *Narramore* v. *Cleveland, CC. & St. L. Ry. Co., supra,* at p. 300, the fact that a statute expressly provides for criminal prosecution as a mode of enforcement does "not exclude the operation of another, and in many respects more efficacious, means of compelling compliance with its terms, to wit, the right of civil action * * *." Certainly, reliance upon the right of civil action by private citizens as a means of insuring compliance with the law is a heritage of our

Anglo-American jurisprudence which should not lightly be restricted. Nor should it be presumed that the Congress intended to restrict the right to recover the damages which under established principles would normally follow from violations of Section 4(a), in the absence of evidence of any such Congressional intention.

2. *Defendants' Acts in Violation of Section 4(a) Were the Legal Cause of Damage to Petitioner.*

(a) *Section 4(a)(6).*

The Circuit Court of Appeals below held that since the damages complained of were not alleged to have resulted from failure to register, there was no legal connection between the violations of Section 4(a)(6) and the loss to petitioner,* and that the only basis upon which the defendants could be held liable would be that their violation of the statute made them liable as insurers against all harm. As an illustration of this point the Court referred to the case of a motorist who, at the moment of a collision, was violating the law by carrying concealed weapons. In such case, of course, the driver does not become liable to a pedestrian injured without negligence merely because he was violating the law at the time of the accident. The Court pointed out that the criminal conduct in that case was without legal significance, since it had no effect in causing the injury (R. fol. 152a, Opinion of C.C.A., pp. 6, 8, footnote 15, p. 6).

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* As has already been shown, the premise of this argument is unsound.

The foregoing illustration, it is submitted, illuminates the error which led the Court below to an incorrect conclusion, for there is no sound analogy between the illustration given and the facts involved in the present case. In this case, the damage to petitioner did not merely occur, without any causal connection, at the same time that the defendants were committing an unlawful act, but, on the contrary, the damage was caused by the very act which was committed in violation of Section 4(a)(6). If the defendants had not caused United to continue to own the securities of its subsidiaries, United would not have suffered the loss in the value of those securities or incurred the expenses entailed by their continued ownership, and the defendants would not have realized the profits which they did as the result of such ownership. In the illustration given by the Court below, the act which violated the statute did not produce the injury. In the present case, it did.

It is therefore not necessary to hold, as stated by the Court below, that the defendants must be held to be insurers against all harm in order for there to be civil liability in this case. All that is required is that they be held liable for damages which their unlawful acts caused to persons within a class designed to be protected by the statute. See *Restatement of Torts*, §286.

Indeed, assuming *arguendo* that the Circuit Court of Appeals was correct in limiting the right of recovery under Section 4(a) by reference to registration under Section 5, it would still appear that even under such a restricted criterion the First Cause of Action of the Amended Com-

plaint sets forth a valid claim for recovery of the profits realized by the defendants. For it alleges that as a result of causing United to own securities, in violation of Section 4(a)(6), the directors, and affiliated banking interests who controlled them, were enabled to realize profits, as they had in the past, from banking and underwriting business which they obtained through their control over United and its holding company system (R. 34a, 35a). If United had been a *registered* holding company there would have been no assurance of realizing such profits, since under Section 17(c) directors who were members of investment banking firms would have been compelled to resign their directorships,* and underwriting fees would have become subject to scrutiny by the Securities and Exchange Commission under its rule relating to competitive bidding. See Rule U-50 of General Rules and Regulations under the Public Utility Holding Company Act of 1935. It would therefore, appear that even if the Amended Complaint failed to state a valid claim for recovery of the *loss* in value of the securities of subsidiaries owned by United, under the restricted criterion enunciated by the Circuit Court of Appeals below, it still would state a valid claim for the recovery of *profits* realized by the defendants as the result of such unlawful ownership. For there profits were realized because United was unregistered, and therefore unregulated. Section 1(c), as has been seen, specifically de-

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* George E. Whitney, Landon K. Thorne, and Hendon Chubb in fact resigned March 28, 1938, the day that United registered (R. 64a, 65a).

clares that an unregulated holding company is injurious to investors.*

(b) *Section 4(a)(3) and (4).*

In addition to the foregoing considerations, which apply both to violations of Sections 4(a)(6) and 4(a)(3) and (4), the following additional considerations are peculiarly applicable to the exchange of securities effected in violation of Section 4(a)(3) and (4).

Section 9(a)(1) makes it unlawful for any *registered* holding company to acquire any securities in any business unless the acquisition has been approved by the Securities and Exchange Commission under Section 10. Under Section 10(a) a person applying for approval of the acquisition of securities must set forth complete information, on Form U 10-1 pursuant to Rule 10A-1, with regard to the security to be acquired, the consideration to be paid there-

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* See also Section 1(b)(4) which states that the interests of investors in the securities of holding companies are or may be adversely affected "when the growth and extension of holding companies bears no relation to economy of management and operation". As stated by this Court in *North American Co.* v. *Securities and Exchange Commission, supra,* at p. 703:

> "The 'growth and extension of holding companies' obviously rest upon their security holdings."

The opinion of the Court further pointed out (at pp. 701-704 706, 710) that the ownership of securities of subsidiaries was the most important single factor in the existence and operation of holding companies, giving rise to a multitude of evils and abuses. It is the number and complexity of the hazards which result from violation of Section 4(a) which differentiates that section from the simpler statutes involved in the cases referred to in the opinion below of the Circuit Court of Appeals (R. fol. 152a, Opinion of C. C. A., p. 6, footnote 14). Section 4(a) was not directed against only one specific hazard, as were the statutes in those cases.

for, a description of the rights and privileges of all securities of the company whose security is to be acquired, options in respect of any such securities, the names of all security holders owning more than 1% of any class of securities of such company, balance sheets and profit and loss statements, and all other pertinent information. Under Section 10(b) the Commission approves the acquisition unless it finds that it will tend toward interlocking relations or concentration of control detrimental to the interest of investors or that the consideration paid in connection with such acquisition is unreasonable or that such acquisition will unduly complicate the holding company system and be detrimental to the interest of the investors. Section 10(c) provides that notwithstanding the provisions of Section 10(b), the Commission shall not approve an acquisition of securities which is detrimental to the carrying out of the provisions of Section 11 or the acquisition of securities of a public utility or holding company unless the Commission finds that such acquisition will serve the public interest by tending toward the economic development of an integrated public utility system. Section 10(e) empowers the Commission to condition its approval of an acquisition upon such terms and conditions, including the price to be paid for such securities, as it may find necessary or appropriate for the protection of investors.

Section 12(d) makes it unlawful for any *registered* holding company to sell any security of any public utility company in contravention of the Commission's rules regarding consideration, fees, disclosure of interest, and similar matters. Section 12(e) makes the solicitation of proxies or consents regarding any security of a subsidiary company

unlawful if made in contravention of the Commission's rules and regulations. Section 12(f) makes it unlawful for any *registered* holding company or subsidiary to enter into any transaction, not otherwise unlawful, with any company in the same holding company system, in contravention of the Commission's rules regarding financial information disclosure of interest and similar matters. Section 12(g) contains corresponding provisions with respect to any affiliate of any public utility company or of any registered holding company or subsidiary.

By causing United to remain unregistered, the defendants deprived the stockholders of United of the protection which they would have received from the foregoing sections if United had been a registered holding company. If the exchange of stock involved in the Mohawk-Niagara merger had been subjected to the requirements of full disclosure and Commission scrutiny and approval, the transaction might never have been consummated and the consequent loss to the stockholders of United might never have occurred. The Second Cause of Action does not and could not allege as a fact what action the Commission would have taken under Sections 9, 10 and 12 if United had been a *registered* holding company. This is obviously unnecessary since United was an unregistered company, and the cause of action is based on violations of Section 4(a)(3) and (4), which applies only to unregistered companies. But the action of the Congress in prohibiting *registered* companies from distributing, exchanging or acquiring securities except in conformity with the exhaustive protective provisions embodied in Sections 9, 10 and 12, gives added emphasis to the fact that the actions of holding companies in effec-

tuating such transactions without the safeguards provided by those sections was one of the evils against which the Act was designed to protect investors. This gives further support to the conclusion that Section 4(a)(3) and (4) was intended to give an investor in the securities of a holding company a right of action for damages resulting from transactions consummated in violation of that section.

The violations of Section 4(a)(3) and (4) fit, in every particular, the criteria set forth in Section 286 of the Restatement of Torts as to when a violation of a statute gives rise to a civil liability. According to that section, a violation of a statute creates civil liability to an individual when (1) the intent of the statute is exclusively or in part to protect the interest of the individual, (2) the interest invaded is one which the statute is intended to protect, (3) where the statute is intended to protect an interest from a particular hazard, the invasion of the interest results from that hazard, and (4) the violation is a legal cause of the invasion. In the present case (1) the intent of the Act is in part to protect investors in the securities of holding companies, such as Petitioner, (2) the interest of such investors in the value of securities of subsidiaries owned by such holding companies is an interest which the Act is intended to protect, (3) the Act is intended to protect them from the hazard of unregulated distributions, acquisitions and exchanges by holding companies of the securities of subsidiary companies, and the invasion of plaintiff's interest resulted from that hazard, and (4) the distribution, acquisition and exchange of securities of subsidiaries of United in violation of the Act is the legal cause of the invasion of Petitioner's interest.

3. *The Limitation of Liability Imposed by the Decision of the Circuit Court of Appeals Allows the Defendants to Retain the Fruits of Their Unlawful Conduct and Gives No Relief to the Stockholders Injured by That Conduct.*

As alleged in the Amended Complaint, the defendants caused United to remain an unregistered company but to perform acts which Section 4(a) expressly forbade such a company to do. By following this course of action, the defendants perpetuated the operations of an unregulated holding company which contributed "nothing" to the normal functioning of the companies in the United holding-company system, which was "economically unnecessary," and which "unduly and unnecessarily" complicated the holding-company system and at the same time assured themselves of a continued "source of underwriting profits and fees" through the domination and control which they continued to maintain over that system through United's ownership of the securities of its subsidiary companies. The stockholders of United "paid a price" for the continued "unnecessary corporate existence" of United and the appropriate remedy for this situation was, as stated by the Securities and Exchange Commission, "dissolution."* The defendants thus continued to enjoy, at the expense of the stockholders of United, the fruits of their domination and control over the United holding-company system as freely as if the Public Utility Holding Company Act of 1935 had never become law. When, as has been shown, cer-

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* The quoted language is from the Findings and Opinion of the Commission, *In the Matter of The United Corporation*, file Nos. 54-33, 59-25, Holding Company Act of 1935, Release No. 4478 dated August 16, 1943 at pp. 8, 27, 28, 43 and 50, 13 S. E. C. 854, at pp. 859, 860, 864, 876, 877, 892, 893 and 899.

tain of the acts of the defendants were unlawful and resulted in damage to the stockholders of United and profits to the defendants, there is no reason why the defendants should not be held civilly liable for their actions, under the established principles of law which have previously been set forth. For, as stated by the Court in *Goldstein* v. *Groesbeck, supra,* at page 427:

> "When the defendants decided to ignore this legislation as unconstitutional, they surely took the risk of answering over to their own stockholders as to the propriety of their action."

POINT II

Section 11(e) imposes a duty upon the directors of an economically unnecessary holding company, which renders no services to its system companies and whose structure does not conform to the standards of Section 11(b), to file a plan of divestment of control, or for the purpose of bringing the company into compliance with the provisions of Section 11(b). A stockholder in such a company has a right of action against directors who fail to perform this duty.

Section 4(b) provides that every holding company with outstanding securities, any of which were distributed through the mails or instrumentalities of interstate commerce subsequent to January 1, 1925 and any of which were owned by non-residents of the State of the company's incorporation on October 1, 1935, "shall register under section 5 on or before December 1, 1935." As alleged in the Third Cause of Action, the defendants caused United to

fail to register from December 1, 1935 to March 28, 1938, in violation of Section 4(b). On the latter date it registered.

Section 11(e) authorized any registered holding company, at any time after January 1, 1936, to submit a plan to the Securities and Exchange Commission for the divestment of control or securities, or for other action to enable the company to comply with the provisions of Section 11(b). The defendants caused United to take no action under Section 11(e) until March 4, 1941, when United filed an alleged "plan" which was disapproved by the Commission in an order which directed United to change its capitalization to one class of stock and to cease to be a holding company. The defendants nevertheless caused United to continue to own well over 10% of the stock of its four subsidiaries. The defendants acted in this manner for purposes of their own profit, with resulting damage to the stockholders of United and profits to themselves.

It is Petitioner's position that it was the duty of the directors and officers of United, under the foregoing sections, to take advantage of the beneficial provisions of the Act by causing United to register and submit itself to the protective regulations of the Act and, after it registered, to submit to the Commission a *bona fide* plan designed to simplify the company's corporate structure and limit the operations of the holding-company system to a single integrated public-utility system, in accordance with the provisions of Section 11(b) and (e). Instead of doing this, they continued, after United had registered as they had previously, to resist and oppose the purposes of the Act designed to protect the interests of investors, in order that J. P. Morgan & Co., Inc., Thorne, Loomis & Co. Inc.,

Thorne, Loomis and other defendants in the banking business might continue to realize profits from the banking and underwriting business they received from United and its subsidiaries.

While this action could not have been legally improper prior to the existence of the Public Utility Holding Company Act of 1935, it is submitted that the enactment of that statute enlarged the fiduciary obligations of the defendants and required that they act for the best interests of security holders as envisaged by the Act rather than in the interests of the affiliated banking interests who dominated and controlled United. One of the major aims of the Act was to eliminate this conflict of interest on the part of directors of holding companies, which experience had shown was injurious to the interests of investors in holding company securities.* In the present case, as alleged in the Third Cause of Action, this same conflict of interest has nevertheless resulted in profits to affiliated banking interests and damage to investors, even after the passage of the Act and the registration of United thereunder. It is submitted that Petitioner, an injured investor, has a right of action against the defendants, whose violations of the fiduciary duties imposed by the Act brought profits to themselves and caused damage to Petitioner.

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* See Reports of Federal Trade Commission and House Committee on Interstate Commerce referred to above at p. 29.

Conclusion

If, as has been shown, the Petitioner has a right of action based on violations of Sections 4(a) or (b) or 11(e), the District Court has jurisdiction over the subject matter of the action* under Section 25 of the Act, and Petitioner was entitled to avail himself of the provisions of that section relating to venue and service of process. It was therefore error for the Circuit Court of Appeals below to affirm the dismissal of the action for lack of subject matter jurisdiction.

Respectfully submitted,

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* Even if the facts alleged in the Amended Complaint also constitute grounds for relief at common law, a federal district court has jurisdiction over the action. *Hurn* v. *Oursler*, 289 U. S. 238; *Armstrong Paint & Varnish Works* v. *Nu-Enamel Corp.*, 305 U. S. 315.

APPENDIX

PUBLIC UTILITY HOLDING COMPANY ACT OF 1935

Necessary for Control of Holding Companies

Section 1. (a) Public-utility holding companies and their subsidiary companies are affected with a national public interest in that, among other things, (1) their securities are widely marketed and distributed by means of the mails and instrumentalities of interstate commerce and are sold to a large number of investors in different States; (2) their service, sales, construction, and other contracts and arrangements are often made and performed by means of the mails and instrumentalities of interstate commerce; (3) their subsidiary public-utility companies often sell and transport gas and electric energy by the use of means and instrumentalities of interstate commerce; (4) their practices in respect of and control over subsidiary companies often materially affect the interstate commerce in which those companies engage; (5) their activities extending over many States are not susceptible of effective control by any State and make difficult, if not impossible, effective State regulation of public-utility companies.

(b) Upon the basis of facts disclosed by the reports of the Federal Trade Commission made pursuant to S. Res. 83 (Seventieth Congress, first session), the reports of the Committee on Interstate and Foreign Commerce, House of Representatives, made pursuant to H. Res. 59 (Seventy-second Congress, first session) and H. J. Res. 572 (Seventy-second Congress, second session) and otherwise disclosed and ascertained, it is hereby declared that the national public interest, the interest of investors in the securities of holding companies and their subsidiary companies and affiliates, and the interest of consumers of electric energy and natural and manufactured gas, are or may be adversely affected—

(1) when such investors cannot obtain the information necessary to appraise the financial position or earning power of the issuers, because of the absence of uniform standard accounts; when such securities are issued without the approval or consent of the States having jurisdiction over subsidiary public-utility companies; when such securities are issued upon the basis of fictitious or unsound asset values having no fair relation to the sums invested in or the earning capacity of the properties and upon the basis of paper profits from intercompany transactions, or in anticipation of excessive revenues from subsidiary public-utility companies; when such securities are issued by a subsidiary public-utility company under circumstances which subject such company to the burden of supporting an overcapitalized structure and tend to prevent voluntary rate reductions;

(2) when subsidiary public-utility companies are subjected to excessive charges for services, construction work, equipment, and materials, or enter into transactions in which evils result from an absence of arm's-length bargaining or from restraint of free and independent competition; when service, management, construction, and other contracts involve the allocation of charges among subsidiary public-utility companies in different States so as to present problems of regulation which cannot be dealt with effectively by the States;

(3) when control of subsidiary public-utility companies affects the accounting practices and rate, dividend, and other policies of such companies so as to complicate and obstruct State regulation of such companies, or when control of such companies is exerted through disproportionately small investment;

(4) when the growth and extension of holding companies bears no relation to economy of management and operation or the integration and coordination of related operating properties; or

(5) when in any other respect there is lack of economy of management and operation of public-utility companies or lack of efficiency and adequacy of service rendered by such companies, or lack of effective public regulation, or lack of economies in the raising of capital.

(c) When abuses of the character above enumerated become persistent and wide-spread the holding company becomes an agency which, unless regulated, is injurious to investors, consumers, and the general public; and it is hereby declared to be the policy of this title, in accordance with which policy all the provisions of this title shall be interpreted, to meet the problems and eliminate the evils as enumerated in this section, connected with public-utility holding companies which are engaged in interstate commerce or in activities which directly affect or burden interstate commerce; and for the purpose of effectuating such policy to compel the simplification of public-utility holding-company systems and the elimination therefrom of properties detrimental to the proper functioning of such systems, and to provide as soon as practicable for the elimination of public-utility holding companies except as otherwise expressly provided in this title.

TRANSACTIONS BY UNREGISTERED HOLDING COMPANIES

SEC. 4. (a) After December 1, 1935, unless a holding company is registered under section 5, it shall be unlawful for such holding company, directly or indirectly—

(1) to sell, transport, transmit, or distribute, or own or operate any utility assets for the transporta-

tion, transmission, or distribution of, natural or manufactured gas or electric energy in interstate commerce;

(2) by use of the mails or any means or instrumentality of interstate commerce, to negotiate, enter into, or take any step in the performance of, any service, sales, or construction contract undertaking to perform services or construction work for, or sell goods to, any public-utility company or holding company;

(3) to distribute or make any public offering for sale or exchange of any security of such holding company, any subsidiary company or affiliate of such holding company, any public-utility company, or any holding company, by use of the mails or any means or instrumentality of interstate commerce, or to sell any such security having reason to believe that such security, by use of the mails or any means or instrumentality of interstate commerce, will be distributed or made the subject of a public offering;

(4) by use of the mails or any means or instrumentality of interstate commerce, to acquire or negotiate for the acquisition of any security or utility assets of any subsidiary company or affiliate of such holding company, any public-utility company, or any holding company;

(5) to engage in any business in interstate commerce; or

(6) to own, control, or hold with power to vote, any security of any subsidiary company thereof that does any of the acts enumerated in paragraphs (1) to (5), inclusive, of this subsection.

(b) Every holding company which has outstanding any security any of which, by use of the mails or any means

or instrumentality of interstate commerce, has been distributed or made the subject of a public offering subsequent to January 1, 1925, and any of which security is owned or held on October 1, 1935 (or, if such company is not a holding company on that date, on the date such company becomes a holding company) by persons not resident in the State in which such holding company is organized, shall register under section 5 on or before December 1, 1935 or the thirtieth day after such company becomes a holding company, whichever date is later.

SEC. 11(e) In accordance with such rules and regulations or order as the Commission may deem necessary or appropriate in the public interest or for the protection of investors or consumers, any registered holding company or any subsidiary company of a registered holding company may, at any time after January 1, 1936, submit a plan to the Commission for the divestment of control, securities, or other assets, or for other action by such company or any subsidiary company thereof for the purpose of enabling such company or any subsidiary company thereof to comply with the provisions of subsection (b). If, after notice and opportunity for hearing, the Commission shall find such plan, as submitted or as modified, necessary to effectuate the provisions of subsection (b) and fair and equitable to the persons affected by such plan, the Commission shall make an order approving such plan; and the Commission, at the request of the company, may apply to a court, in accordance with the provisions of subsection (f) of section 18, to enforce and carry out the terms and provisions of such plan. If, upon any such application, the court, after notice and opportunity for hearing, shall approve such plan as fair and equitable and as appropriate to effectuate the provisions of section 11, the court as a court of equity may, to such extent as it deems necessary for the purpose of carrying out the terms and provisions of such plan, take exclusive jurisdiction and possession of the company or companies and the assets thereof, wher-

ever located; and the court shall have jurisdiction to appoint a trustee, and the court may constitute and appoint the Commission as sole trustee, to hold or administer, under the direction of the court and in accordance with the plan theretofore approved by the court and the Commission, the assets so possessed.

JURISDICTION OF OFFENSES AND SUITS

SEC. 25. The District Courts of the United States, the Supreme Court of the District of Columbia, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have jurisdiction of violations of this title or the rules, regulations, or orders thereunder, and, concurrently with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by, or to enjoin any violation of, this title or the rules, regulations, or orders thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enforce any liability or duty created by, or to enjoin any violation of, this title or rules, regulations, or orders thereunder, may be brought in any such district or in the district wherein the defendant is an inhabitant or transacts business, and process in such cases may be served in any district of which the defendant is an inhabitant or transacts business or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 128 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 225 and 347), and section 7, as amended, of the Act entitled "An Act to establish a court of appeals for the District of Columbia", approved February 9, 1893 (D. C. Code, title 18, sec. 26). No costs shall be assessed for or against the Commission in any proceeding under this title brought by or against the Commission in any court.

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